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OUTLOOK

FOR THE ECONOMY AND REAL ESTATE

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NOVEMBER 1984

OUTLOOK FOR THE ECONOMY AND REAL ESTATE

Aggregate Economy

The economy has experienced a sharp slowdown during the third quarter due to the March to August increase in interest rates. Real or inflation-adjusted Gross National Product (GNP) increased 2.7 percent during the third quarter compared to 7.1 percent in the second quarter and 10.1 percent in the first quarter. The increase in third quarter GNP was due almost entirely to inventory investment as final sales remained virtually unchanged from the second quarter.

Despite this slowdown, it is unlikely that the economy is on the brink of a severe recession. The two primary conditions for a severe bust, a surge of inflation and inventories far in excess of needs to meet current sales, are not present at this time. The rates of increase of both prices and wages have been constant for about a year while inventories at all stages of production and distribution remain low.

Moreover, there are numerous indications that the economy is reaccelerating in response to the decline in interest rates over September and October:

- The Index of Leading Economic Indicators rose 0.4 percent in September following three consecutive monthly declines.
- Retail sales were up 1.6 percent in September after falling in July and August.
- Housing starts increased 9 percent in September with increases occurring in every region of the country.
- Domestic auto producers expect to operate near capacity for at least the remainder of the fourth quarter to meet increased sales and build inventories.

This reacceleration should result in real GNP growth of about 2 1/2 percent for the fourth quarter of 1984 and the first quarter of 1985. Then the economy should enter a two to three quarter transition period of sluggish and erratic growth with declining housing starts and slower growth of both consumption spending and business investment spending. By 1986 the recovery should resume but at a more moderate and sustainable pace.

Employment and Inflation

The civilian unemployment rate held at 7.4 percent in October, virtually the same level as September, August, and July, despite a large increase in total employment over the month. As measured by non-agricultural payrolls, total employment rose by 440,000 in October compared to increases of 231,000 in September and 173,000 in August. The unemployment rate may drop another one or two tenths of a percent in the next few months but should begin rising again in 1985 as the economy enters a growth recession where the growth of the economy is too slow to absorb all new entrants into the labor force.

The Consumer Price Index (CPI) increased at a compound annual rate of 3.6 percent during the third quarter, down slightly from the 3.7 percent annual rate of the second quarter. Inflation should remain low through 1985 due to moderate wage increases, stable energy prices, declining food prices, and a strong dollar which keeps import prices low and thereby restrains price increases domestically produced goods and services. For all of 1985 the CPI should increase just for 4 percent, down slightly from the 1984 level. However, as the recovery resumes in 1986 the rate of inflation should accelerate to the five percent level.

Monetary Policy and Interest Rates

Both short- and long-term interest rates continued to decline in October due to relatively weak private credit demand and a more accomodative stance by the Federal Reserve Board (FED). In response to the sharp slowdown of the economy, the FED has been aggressively supplying reserves to the banking system since early September. In response, the federal funds rate has fallen from an average of 11.7 percent during the first week of September to an average of 9.5 percent during the last week of October. Over the same period yields on 3-month Treasury bills have declined from 10.6 percent to 9.3 percent while most major banks reduced their prime lending rate from 13 percent to 12 percent. Long-term rates have also declined with the yield on 30-year Treasury bonds falling 100 basis points to 11.7 percent.

Interest rates are likely to rise slightly later this quarter and into the first quarter of 1985 in response to a temporary increase in total credit demand:

- Business loans outstanding should continue the increase begun in September following an actual decline in August.

- A large volume of offerings of corporate bonds are expected over this period.

- Consumer loan demand should be strong as domestic auto sales return to the 8 million unit annual rate.

- Treasury borrowing requirements should average about $60 billion during the last quarter of this year and the first quarter of 1985 compared to about $20 billion during the second quarter of 1984 and $40 billion during the third quarter.

After this temporary increase is passed, the reduced credit demands associated with the much slower economic growth of 1985 should allow interest rates to trend downward over the remainder of that year. By the final quarter of 1985 the yield on three month Treasury bills should be about 8.8 percent while the interest rate on 30-year, fixed-rate mortgage loans should be down to about 13 percent.

Real Estate Markets

Existing home sales fell 1.1 percent in September to a seasonally adjusted annual rate of 2.67 million units in response to high mortgage interest rates. This marks the fifth consecutive monthly decline from the previous peak of 3.07 million units of April. Housing starts rose 9 percent in September to a seasonally adjusted annual rate of 1.68 million units.

As is typical of this time of year, the median price of existing single-family homes sold in September declined $1,100 from the August level to $72,600. This price decline along with a rise in the median family income boosted the National Association of Realtors' Affordability Index 0.7 percentage points to 84.4. This means that a family earning the median income had 84.4 percent of the income needed to qualify to purchase the median-priced existing home.

Both resales and starts should decline modestly from current levels over 1985 due to slow growth of employment and income and continued high interest rates. Resales should total about 2.6 million units for all of 1985 and then rise to about 2.9 million units in 1986. Housing starts should total about 1.6 million units in 1985 and then rise to about 1.8 million units in 1986.

The rate of growth of construction of new commercial space should continue to trend downward through 1985 due to much reduced levels of investment in new office space. For all of 1985, new commercial building construction should increase just 7 percent compared to an expected increase of 33 percent from 1984. In contrast, the rate of growth of construction of new industrial buildings should increase to about 15 percent in 1985 from an expected increase of about 12 percent for 1984.

Table 1

NOVEMBER 1984

U.S. ECONOMIC OUTLOOK

	QUARTERS								YEARS				
	Actual	Forecast							Actual		Forecast		
	84:3	84:4	85:1	85:2	85:3	85:4	86:1	86:2	1982	1983	1984	1985	1986
AGGREGATE ECONOMY													
Gross National Product ($ billions)	3,701	3,760	3,825	3,861	3,892	3,953	4,026	4,109	3,069	3,305	3,665	3,883	4,157
Percent Change	6.3	6.5	7.1	3.7	3.3	6.4	7.6	8.5	3.8	7.7	10.9	5.9	7.1
Percent Change (without inflation)	2.7	2.5	2.5	0.0	-0.4	1.8	2.8	3.5	-2.1	3.7	6.8	1.9	2.4
Consumption	0.2	5.3	3.4	1.8	1.1	1.5	2.2	2.8	1.4	4.8	5.3	2.9	2.2
Durables	-3.6	11.4	4.1	-0.6	-2.4	0.0	2.4	3.8	-0.3	12.1	12.9	2.9	1.8
Nondurables	-0.5	4.9	2.9	2.0	1.5	1.4	1.7	2.0	0.6	3.7	5.0	2.9	1.8
Services	2.1	3.5	3.4	2.5	2.0	2.2	2.6	3.0	2.5	3.4	3.0	2.9	2.6
Residential Investment	2.7	-9.1	-3.8	-5.0	1.9	4.1	6.8	8.9	-15.0	41.7	12.9	-2.8	5.5
Nonresidential Investment	7.9	4.7	5.4	5.1	3.0	1.8	2.5	2.3	-4.7	2.5	18.7	5.9	2.8
Structures	1.8	1.6	4.0	4.2	1.8	0.8	2.8	3.0	0.2	-7.8	14.5	3.8	2.9
Equipment	10.5	5.8	6.0	5.4	3.5	2.2	2.4	2.1	-6.8	7.3	20.5	6.7	2.8
Exports	16.1	6.4	4.9	5.0	4.6	4.2	4.9	6.1	-7.8	-5.6	6.2	6.1	5.3
Imports	49.8	5.6	5.4	5.2	2.5	2.1	2.2	2.5	1.3	7.6	29.5	9.5	2.6
Government Purchases	8.6	3.3	3.0	3.4	2.6	1.0	1.7	1.5	2.0	-0.3	3.7	4.5	1.7
Consumption (% of GNP)	64.5	65.0	65.1	65.4	65.6	65.6	65.5	65.4	65.1	65.8	64.8	65.4	65.3
Residential Investment (% of GNP)	3.7	3.6	3.5	3.5	3.5	3.5	3.6	3.6	2.6	3.5	3.7	3.5	3.6
Nonresidential Investment (% of GNP)	12.5	12.6	12.7	12.8	13.0	13.0	12.9	12.9	11.3	11.1	12.4	12.9	12.9
Structures (% of GNP)	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.6	3.2	3.4	3.5	3.5
Equipment (% of GNP)	9.1	9.1	9.2	9.3	9.4	9.4	9.4	9.4	7.7	7.9	8.9	9.4	9.4
Inventory Change ($ billions)	72.4	57.6	51.5	30.4	8.5	9.8	12.8	17.7	-26.1	-13.5	63.6	25.1	19.8
Mfg. Capacity Utilization Rate (%)	83	82	82	82	81	80	80	80	71	75	82	81	81
Auto Sales (millions of units)	10.3	11.0	10.9	10.7	10.5	10.4	10.3	10.3	8.0	9.2	10.6	10.6	10.4
Domestic (% of total)	77.3	73.4	77.1	76.6	73.4	72.4	72.5	72.4	72.3	74.0	76.5	74.9	71.9
Imported (% of total)	22.7	26.6	22.9	23.4	26.6	27.6	27.5	27.6	27.9	26.0	23.5	25.1	28.1
Manufacturing Industrial Production (% change)	7.2	1.7	2.4	0.7	-1.9	0.5	2.5	4.1	-8.5	7.8	11.4	2.2	2.3
Common Market	8.9	3.6	4.6	2.8	3.5	2.1	1.1	3.1	-1.4	0.7	2.9	3.3	2.2
Japan	5.3	8.9	8.7	3.0	2.6	1.3	1.4	2.4	0.4	3.5	10.5	6.0	2.1
Employment(millions)(civilian:household basis)	105.2	106.1	106.6	106.9	107.0	107.3	107.7	108.1	99.5	100.8	105.0	107.0	108.5
Unemployment Rate (%) (civilian)	7.5	7.3	7.3	7.5	7.8	7.9	8.0	8.1	9.7	9.6	7.5	7.6	8.0
Personal Income per Household (average)<1>	38,965	39,550	40,199	40,532	40,854	41,438	42,146	42,899	33,690	35,447	38,578	40,756	43,265
Percent Change -- Year Ago (w/o inflation)	5.9	4.6	3.4	1.9	1.0	0.8	0.6	1.3	-0.5	1.4	5.3	1.8	1.5
Personal Taxes per Household (average)	7,059	7,181	7,296	7,364	7,428	7,558	7,683	7,851	6,441	6,484	6,971	7,412	7,934
Percent Change -- Year Ago (w/o inflation)	6.4	5.6	4.2	2.6	1.2	1.1	1.1	2.1	-2.2	-3.1	3.6	2.3	2.4
Percent of Personal Income	18.9	18.9	19.0	19.0	19.0	19.1	19.1	19.1	19.9	19.1	18.9	19.0	19.2
Disposable Income per Household (average)	31,907	32,369	32,904	33,168	33,426	33,880	34,465	35,048	27,249	28,964	31,607	33,344	35,331
Percent Change--Year Ago (w/o inflation)	5.7	4.4	3.3	1.8	1.0	0.8	0.6	1.2	-0.1	2.5	5.7	1.7	1.4
Household Interest Payments (% of total)	10.5	10.3	10.3	10.4	10.7	10.6	10.4	10.3	9.6	9.8	10.4	10.5	10.2
Net Worth per Household (average)	77,375	79,136	80,680	82,194	83,684	85,329	87,253	89,327	66,177	73,908	77,075	82,972	90,467
Percent Change -- Year Ago (w/o inflation)	-0.6	1.3	2.6	3.9	4.0	3.6	3.9	4.1	-1.8	7.6	0.5	3.5	4.3
Consumer Price Inflation (CPI)	3.6	4.2	4.1	4.0	3.9	4.3	5.0	5.1	6.2	3.2	4.3	4.0	4.7
Gross National Product Inflation (GNP Deflator)	3.6	3.9	4.5	3.7	3.7	4.5	4.7	4.9	6.0	3.8	3.8	4.0	4.6
Personal Consumption Inflation	4.5	3.7	3.7	3.8	3.8	4.1	4.8	4.9	5.9	3.7	3.3	3.7	4.5
Residential Construction Inflation	-0.3	0.8	4.0	4.3	4.3	4.9	6.0	6.4	3.0	1.7	3.3	3.4	5.7
Nonresidential Construction Inflation	2.8	3.4	5.3	5.5	5.7	6.3	6.9	7.1	4.9	-1.0	0.5	4.5	6.7
Producers Price Inflation (WPI)	-0.7	1.5	1.8	2.4	2.7	4.5	5.0	5.0	2.0	1.3	2.5	1.9	4.5
Compensation per Manhour (% change)	3.4	5.1	6.7	5.4	5.4	6.1	7.0	6.3	8.0	4.8	4.2	5.3	6.3
Productivity (% change)	2.3	2.2	1.4	1.4	1.1	1.3	1.1	1.6	0.2	3.4	3.0	1.8	1.3
Unit Labor Cost (% change)	0.8	2.9	5.2	3.9	4.2	4.7	5.8	4.7	7.8	1.3	1.2	3.4	4.9
Unit Capital Cost (% change)	4.5	4.4	4.2	4.0	3.8	3.5	3.3	3.1	9.5	6.9	4.6	3.9	3.1
Before Tax Corporate Profits ($ billions)<2>	240	242	237	230	220	219	222	228	181	213	247	226	233
Corporate Tax Liability	95	98	96	91	84	83	86	89	76	86	99	88	92
After Tax Profits	145	144	141	139	136	136	136	139	105	127	147	138	141
Inventory Valuation Adjustment	-1	-4	-9	-12	-15	-20	-24	-25	-9	-11	-6	-14	-26
Capital Consumption Adjustment	59	63	72	76	80	84	85	86	3	33	55	78	86
Profits from Current Production (with IVA, CCA)	203	203	204	203	201	200	197	200	98	149	196	202	202
Adjusted for Inflation (84:1 base)	200	197	197	194	190	187	182	183	105	153	194	192	183
Percent Change - Year Ago	22.2	11.1	6.5	0.2	-5.1	-5.2	-7.6	-5.8	-14.6	46.0	26.8	-1.0	-4.5
Per Unit of Output (% of GNP)	5.5	5.4	5.3	5.3	5.2	5.1	4.9	4.9	3.2	4.5	5.4	5.2	4.9
Effective Corporate Tax Rate (%)<2>	30	31	31	30	28	28	29	30	39	34	32	29	30
Federal Tax Receipts (Unified basis)	710	647	653	831	733	674	666	919	609	613	681	723	773
Percent of GNP	19.2	17.2	17.1	21.5	18.8	17.1	16.5	22.4	19.8	18.6	18.6	18.6	18.6
Federal Expenditures (Unified basis)	844	892	930	943	932	966	993	1,005	740	803	855	943	1,014
Percent of GNP	22.8	23.7	24.3	24.4	23.9	24.4	24.7	24.5	24.1	24.3	23.3	24.3	24.4
Surplus or Deficit (Unified basis)	-134	-245	-276	-112	-199	-292	-327	-86	-131	-190	-174	-220	-241
% of GNP	3.6	6.5	7.2	2.9	5.1	7.4	8.1	2.1	4.2	5.8	4.7	5.7	5.8
% of Personal Savings	81.4	159.9	173.2	73.1	132.6	185.1	194.4	49.4	97.8	158.1	112.9	141.0	139.3
% of Net Domestic Savings	40.1	75.5	83.5	35.0	64.1	92.9	101.8	25.9	67.3	80.0	54.1	68.9	72.5

<1> Includes personal contributions for social insurance.
<2> Adjusted to include impact of windfall profits tax on domestic crude oil production.

Source: Model developed by the NATIONAL ASSOCIATION OF REALTORS, and Data Resources, Inc.
Assumptions and simulations by Dr. Jack Carlson, Hugh Graham, and Dick Peach.

Table 2

NOVEMBER 1984

REAL ESTATE AND FIANNCIAL MARKETS

	QUARTERS								YEARS				
	Actual	Forecast							Actual		Forecast		
	84:3	84:4	85:1	85:2	85:3	85:4	86:1	86:2	1982	1983	1984	1985	1986
REAL ESTATE MARKETS													
Existing Single-Family Home Sales (thousands)	2,713	2,713	2,699	2,620	2,557	2,522	2,655	2,847	1,948	2,719	2,851	2,600	2,901
Percent Change - Year Ago	-2.1	-1.6	-8.2	-13.7	-5.7	-7.0	-1.6	8.7	-17.2	39.6	4.8	-8.8	11.6
Dollar Volume (billions)	237.0	233.0	234.6	231.2	226.5	221.2	237.4	260.2	156.5	224.5	245.7	228.4	264.5
Existing Home Prices - Median ($1000's)	73.6	73.0	74.4	76.0	76.6	76.1	77.9	79.7	67.7	69.8	72.9	75.8	79.6
Percent Change - Year Ago	3.6	4.2	3.7	3.9	4.1	4.3	4.6	4.9	2.3	3.2	4.4	4.0	5.0
Monthly Mortgage Payment (P&I, 80%, 30 yr.)	704	664	673	672	664	645	655	671	754	633	671	663	669
Percent of Household Income	23	21	21	21	20	20	20	20	28	22	22	20	19
NAR Affordability Index	83.9	87.5	86.1	84.5	83.9	86.8	87.0	87.5	68.4	82.0	86.1	85.3	88.2
New Single-Family Home Sales (thousands)	616	641	600	570	590	610	635	670	417	626	645	592	672
Percent Change - Year Ago	4.9	-4.6	-13.3	-9.9	-4.2	-4.9	5.9	17.6	-4.3	50.1	3.1	-8.2	13.5
New Home Prices - Median ($1000's)	81.4	81.7	82.5	83.4	84.3	85.5	86.8	88.3	69.3	75.5	80.4	83.9	89.1
Percent Change - Year Ago	4.8	7.7	5.9	3.7	3.6	4.6	5.3	6.0	0.7	8.9	6.5	4.4	6.2
New Home Prices--Mean ($1000's, Quality Adjusted)	94.9	93.3	94.5	95.5	98.0	97.4	99.1	100.7	87.8	89.7	93.2	96.4	101.8
Percent Change - Year Ago	4.6	3.4	3.8	2.2	3.3	4.4	4.9	5.4	2.8	2.1	3.9	3.4	5.7
New Mortgage Commitments ($ billions)	166.3	155.4	152.4	150.7	151.2	153.1	158.4	173.3	64.8	163.4	179.9	151.8	177.9
Percent Change - Year Ago	-13.4	-5.3	-20.3	-27.0	-9.1	-1.4	4.0	15.0	8.1	152.1	10.1	-15.6	17.2
Mortgage Debt Outstanding ($ billions)	1,998	2,074	2,150	2,225	2,300	2,376	2,293	2,241	1,629	1,752	1,967	2,263	2,237
Homeowners' Equity ($ billions)	2,731	2,787	2,830	2,854	2,878	2,913	2,956	3,007	2,336	2,519	2,714	2,869	3,039
Housing Inventory (millions)	91.3	91.7	92.0	92.4	92.7	93.0	93.4	93.7	88.5	89.6	91.1	92.5	93.9
Private Housing Starts (thousands)	1,656	1,652	1,636	1,635	1,618	1,670	1,747	1,807	1,056	1,704	1,793	1,640	1,798
Single-Family	977	1,025	1,007	1,011	1,015	1,081	1,102	1,146	663	1,066	1,104	1,028	1,145
Percent of Total	59.0	62.1	61.6	61.8	62.7	64.7	63.1	63.4	62.8	62.6	61.5	62.7	63.7
Multi-Family	679	627	628	624	603	589	645	661	394	637	688	611	653
Percent of Total	41.0	37.9	38.4	38.2	37.3	35.3	36.9	36.6	37.2	37.4	38.5	37.3	36.3
Mobile Home Shipments (thousands)	304	307	311	309	308	297	302	302	240	296	301	306	300
Rental Vacancy Rate (%)	5.5	5.4	5.4	5.4	5.4	5.4	5.4	5.4	5.3	5.6	5.5	5.4	5.4
Unsold New Homes (% of sales)	58.2	60.2	59.8	57.1	54.5	53.2	52.7	53.2	65.2	43.0	52.7	56.1	54.1
Office Vacancy Rate (%)<1>	11.5	11.1	10.7	10.4	10.1	9.9	9.7	9.5	8.0	11.7	12.3	10.3	9.5
Industrial Vacancy Rate (%)<1>	4.4	4.2	4.0	3.9	3.8	3.8	3.7	3.7	4.4	4.9	4.5	3.9	3.6
New Commercial Building Construction (% Ch Value)	2.8	3.4	3.6	4.5	2.4	8.7	14.1	13.3	9.0	-4.2	32.8	6.8	10.7
New Industrial Building Construction (% Ch Value)	-2.8	37.5	15.1	15.1	9.5	8.2	8.4	9.6	2.5	-25.7	11.5	15.4	10.3
FIANNCIAL MARKETS													
Money Supply													
M1 (% change)(FED Target 4-8%)	4.6	3.0	4.3	5.0	6.2	7.5	6.0	5.9	6.6	11.0	6.6	4.8	6.3
M1 Velocity (% change)	1.7	3.5	2.7	-1.2	-2.7	-1.0	1.5	2.4	-2.6	-3.1	4.0	1.1	0.7
M2 (% change)(FED Target 6-9%)	6.2	6.4	6.6	6.5	8.1	8.9	7.6	7.2	9.5	12.6	7.5	6.9	7.6
M2 Velocity (% change)	0.1	0.1	0.5	-2.6	-4.5	-2.3	0.1	1.2	-5.3	-4.4	3.2	-0.9	-0.6
Monetary Base (% change)	7.9	4.5	5.8	5.0	4.5	4.8	5.7	6.2	6.9	9.5	8.3	5.6	5.6
Flow of Funds													
Supply (total)	456	442	443	432	423	431	438	451	212	280	426	432	454
Personal Savings	165	153	160	153	150	158	168	174	136	118	154	155	173
Savings Rate	6.3	5.8	5.9	5.6	5.4	5.6	5.9	6.0	6.2	5.0	6.0	5.6	5.9
Net Business Savings	122	119	118	115	110	107	102	103	29	76	116	112	104
State + Local Govt. Savings	47	52	53	52	50	50	51	54	33	44	52	51	55
Foreign Funds(current account deficit)	122	117	112	113	114	116	117	120	13	42	104	114	121
Demand (total)	399	404	423	238	325	418	468	244	165	325	411	351	405
Consumer Installment Debt(net change)	76	45	33	18	17	17	19	23	19	40	72	21	26
Commercial+Industrial Loans(net change)	50	21	19	16	15	13	21	29	22	-2	45	16	32
Home Mortgage Debt(net change)	139	94	94	92	95	96	102	106	-6	96	121	94	106
Federal Deficit	134	245	276	112	199	292	327	86	131	190	174	220	241
Selected Interest Rates (Percent)													
Mortgage Commitment Rates													
30 Year,Fixed-Rate	14.7	14.0	13.9	13.6	13.3	13.0	12.9	12.9	17.2	13.9	14.2	13.4	12.9
Real Mortgage Rate	11.2	10.1	9.4	9.9	9.6	8.5	8.2	8.0	12.9	10.2	10.3	9.4	7.9
1 Year ARM (without buy-down)	13.5	12.5	12.3	11.9	11.6	11.5	11.4	11.5	14.0	11.3	12.8	11.8	11.5
Real Mortgage Rate	9.9	8.5	7.7	8.2	8.0	7.1	6.7	6.6	9.7	7.5	9.0	7.7	6.5
Corporate Bond Rate (AAA)	13.0	12.3	12.4	12.0	11.7	11.4	11.3	11.2	13.8	12.0	12.7	11.9	11.3
Government Bond Rate	12.8	12.0	11.9	11.6	11.1	10.8	10.6	10.5	12.9	11.3	12.5	11.4	10.6
Real Government Bond Rate	9.3	8.0	7.4	7.9	7.5	6.3	6.0	5.6	8.7	7.6	8.7	7.3	5.6
Federal Funds Rate	11.4	10.1	10.4	10.0	9.7	9.7	9.6	9.8	12.3	9.1	10.4	10.0	9.9
3 Month Treasury Bill Rate	10.3	9.6	9.5	9.2	8.9	8.8	8.7	8.9	10.6	8.6	9.7	9.1	8.9
Real 3 Month T-Bill Rate	6.7	5.7	4.9	5.4	5.2	4.4	4.1	4.0	6.4	4.8	5.9	5.0	3.9
1 Year Treasury Bill Rate	11.8	10.8	10.6	10.2	9.9	9.8	9.7	9.8	12.3	9.6	11.1	10.1	9.8
Commercial Paper Rate	11.1	10.1	10.2	9.8	9.5	9.5	9.4	9.6	11.9	8.9	10.3	9.8	9.7
Rate on Money Market Fund Shares	11.3	10.3	10.4	10.0	9.6	9.6	9.6	9.8	12.1	9.0	10.5	9.9	9.9
Prime Rate	13.0	12.2	11.9	11.9	11.9	11.4	11.4	11.4	14.9	10.8	12.1	11.8	11.6

<1> Historical data courtesy of Coldwell Banker.

Source: Model developed by the NATIONAL ASSOCIATION OF REALTORS, and Data Resources, Inc.
Assumptions and simulations by Dr. Jack Carlson, Hugh Graham, and Dick Peach.

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OUTLOOK

FOR THE ECONOMY AND REAL ESTATE

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DECEMBER 1984

Outlook For The Economy and Real Estate

Aggregate Economy

The strong growth in real output during the first half of this year has been replaced by slower less eratic growth as demand conditions weakened due to the existence of high real interest rates earlier this year. Third quarter growth in real GNP has been revised downward from 2.7 percent to 1.9 percent. The smaller than expected increase in third quarter growth, despite a rise of 5.9 percent in domestic demand, can be attributed to a slowdown in personal consumption expenditures and a large increase in imports. Underscoring this slowing trend has been a decline in factory orders and durables in October. Howevever, retail sales as well as construction expenditures are expected to increase in November, an indication that lower interest rates will help to stimulate the economy and sustain economic growth in the fourth quarter. Fourth quarter growth in real GNP is projected to be 2.0 percent leaving overall growth for all of 1984 at 6.7 percent.

Real GNP growth should remain around 2.0 percent for the first quarter of 1985 before declining to 1.1 percent by the second quarter. This small downturn in the middle of 1985 represents a transistion period before the next acceleration begins by the fourth quarter of 1985 when real GNP growth should climb to 2.6 percent. Unlike past downturns, this one will be very small and short. Prospects of a recession are unlikely as the economy is not expected to experience labor shortages, spiraling interest rates or falling plant capacity; occurences that ususally precede a slump. Instead, leaner inventories and lower real interest rates will be major factors in buffering the economy from any serious declines in output. During past downturns, existence of large inventories during a period of declining output has increased costs therefore absorbing funds that could have been used for much needed investment. The trend toward leaner inventories will avoid this problem. In addition, lower real interest rates resulting from expansionary fiscal and monetary policies will stimulate demand in interest sensitive industries thus partially offsetting declines in output.

Foreign producers continue to absorb the rising share of U.S. spending while domestic producers continue to suffer losses. Imports, increasing to 26.1 percent of capital spending in the third quarter of 1984 compared to 15.7 percent in 1980, will continue to erode U.S. output. Continued import penetration is expected to hold down real growth in output til mid - 1985 by squeezing profits, reducing employment, and depressing capital goods spending in manufacturing industries; consequently, pushing down interest rates even further. However, the continued downward trend in interest rates will trigger a resurgence in demand for residential construction, automobiles and household durables. The rebound in these industries would eventually boost capital spending only after a one or two period lag allowing for profits and confidence to improve.

Employment and Inflation

The overall unemployment rate declined 0.3 percent in November to 7.0 percent, the sharpest drop since June. In addition, total employment rose by nearly 300,000 jobs with most of the growth in the service sectors. The improvement in the employment figures represents the stimulative effect recent declines in interest rates has had on the economy and reinforces confidence

that the present slowdown will be temporary and not result in a recession. Unemployment for all of 1984 is expected to be 7.6 percent, two percentage points below the 1983 annual rate. The jobless rate is expected to increase slightly into 1985 as real output growth continues to slow slightly and reach 8 percent by the end of next year.

The consumer price index increased on a seasonally adjusted basis by 0.4 percent in October, this is equivalent to a compound annual rate of 4.9 percent and is the same as the September rise. Declines in food and fuel prices continue to be the major factors restraining inflation, while prices of non-energy services (which comprise 35 percent of the index) have been increasing at a faster pace since the beginning of 1983. The consumer price index for all of 1984 is expected to increase 4.3 percent. Inflation is expected to increase at a modest 4.0 percent annual rate through 1985 as oil prices are expected to decline further in response to the weak global recovery. The continued strength of the dollar will keep down import prices as well as the prices of their competitors in the domestic market. Although, the value of the dollar will decline slightly into 1985 as represented by a decline in the trade-weighted exchange rate, it will still remain well above its 1983 levels thus it is still "strong" relative to other currencies. The trade- weighted exchange rate is a new addition to the forecast table and represents a weighted index with a base year of 1967 of the U.S. dollar against foreign currency.

Monetary Policy

The federal reserve in response to an unexpectedly strong downturn in economic growth for the third quarter and modest levels in the rate of inflation began a more accomodative monetary policy in early September in an attempt to stabilize the economy. They aggressively supplied reserves to the banking system thus increasing the supply of loanable funds and pushing the Federal Funds rate to 9 percent. The slower growth in private credit demands in addition to the increase in loanable funds has removed the upward pressure on interest rates allowing them to decline substantially. Since peaking in August, short term rates have declined 165 basis points to 8.7 percent in November. Reflecting lower inflationary expectations, long term rates have declined almost 200 basis points to 11.5 percent in November from their June peaks. In addition, the term structure of interest rates has also flattened significantly -- the spread between long term and short term rates is 60-130 basis points lower then the June rates. This is another indication that confidence about future price trends is improving. Further signs of a loosening grip by the Federal Reserve include a reduction in the discount rate to 8-1/2 percent compared to 9 percent in early September. Major banks have responded by cutting their prime lending rates to 11-1/2 percent in November. This has been the fifth reduction in the prime since late September.

Over the forecast interval, further easing measures by the Federal Reserve are expected including a reduction in its discount rate to 8 percent by the end of this year. Both short and long term rates are expected to slowly decline through 1985 til the middle of 1986. Once private credit demands rebound in response to these lower interest rates and the deficit continues to absorb the supply of loanable funds interest rates will begin to trend upward by the middle of 1986.

Real Estate Markets

The housing industry is experiencing modest gains as lower interest rates has improved affordability for homebuyers. It is estimated that for every one percent decline in real interest rates (after adjusting for inflation), 400,000 to 500,000 more families are able to satisfy their housing needs. Underscoring the strong pent up demand for housing that has existed due to high real interest rates during the first half of this year was a leveling off of resales in October after five months of decline. Resales for all of 1984 are expected to total 2.8 million units. As interest rates continue to decline, resales are expected to trend upward through 1985 reaching the 2.7 million units for all of 1985. Housing starts, which declined 9.8 percent in October, have been quite volatile and are also expected to begin to trend upward through 1985 in response to an improvement in affordability.

Conventional and adjustable rate mortgages continue to decline. Fixed rate mortgages declined 54 basis points to 14.16 percent in November over October's rate while adjustable rates have been declining more slowly by 35 basis points to 12.49 percent. As bond yields continue to trend downward, mortgage rates are expected to follow suit although at a slower pace. Fixed rate mortgages should decline to 13 percent by the end of 1985. Adjustable rate mortgages are expected to fall to 10.8 percent. Lower interest rates will translate into a lower payment to income ratio and will therefore make homeownership relatively less costly in 1985.

Prices of resales are expected to increase at a pace equal to or slightly above overall inflation through next year, while new home prices are likely to accelerate slightly faster. The median existing single-family home price should be about $73,600 for the fourth quarter of this year; 3.6 percent above the median a year earlier. The median is likely to increase 4.3 percent by the end of 1985 to $76,800, a rate slightly faster than the rate of inflation. This year new single family home prices for the fourth quarter will increase 3.3 percent from a year earlier to $80,200. Rising faster than inflation, the median new-home price is expected to increase an additional 4.7 percent to $84,500 by the end of 1985.

The current decline in construction of new commercial space is expected to continue through the first quarter of next year in response to the slower pace in the residential market during the third quarter. Commercial construction activity should gradually increase by the second quarter of next year as lower interest rates makes investment in these areas more attractive. Despite the current slowdown, commercial construction activity for 1984 is likely to be nearly 34 percent higher than in 1983. This construction activity should increase about 5.6 percent in 1985 and an additional 13.3 percent in 1986.

In contrast, new industrial building construction activity, which is now running about 23 percent ahead of last year's fourth quarter, should gradually slow next year. By the fourth quarter of 1985, the growth rate of industrial building construction is likely to be about 6 percent.

Table 1

DECEMBER 1984

U.S. ECONOMIC OUTLOOK

	QUARTERS								YEARS				
	Actual	Forecast							Actual		Forecast		
	84:3	84:4	85:1	85:2	85:3	85:4	86:1	86:2	1982	1983	1984	1985	1986
AGGREGATE ECONOMY													
Gross National Product ($ billions)	3,695	3,749	3,807	3,852	3,892	3,962	4,038	4,132	3,069	3,305	3,660	3,878	4,179
Percent Change	5.7	5.9	6.3	4.9	4.2	7.4	7.9	9.7	3.8	7.7	10.8	5.9	7.8
Percent Change (without inflation)	1.9	2.0	2.0	1.1	0.4	2.6	2.9	4.6	-2.1	3.7	6.7	2.0	3.0
Consumption	0.6	4.1	3.9	2.8	2.2	1.8	2.3	3.1	1.4	4.8	5.3	3.2	2.6
Durables	-2.2	8.8	5.4	2.6	1.8	0.0	2.2	4.3	-0.3	12.1	12.9	4.1	2.8
Nondurables	-1.3	2.4	3.5	2.8	2.3	2.1	2.0	2.6	0.6	3.7	4.7	2.7	2.4
Services	3.1	3.9	3.6	2.8	2.3	2.3	2.5	3.0	2.5	3.4	3.2	3.2	2.7
Residential Investment	-4.5	-5.6	-0.9	3.2	6.1	4.7	6.5	6.5	-15.0	41.7	12.2	-0.2	6.4
Nonresidential Investment	15.8	4.4	1.3	0.7	0.8	2.2	3.7	6.0	-4.7	2.5	19.8	4.6	3.9
Structures	7.0	2.2	1.0	0.9	1.8	3.4	7.5	8.8	0.2	-7.8	15.3	3.3	5.8
Equipment	19.6	5.3	1.4	0.6	0.4	1.8	2.3	5.0	-6.6	7.3	21.7	5.1	3.1
Exports	8.8	8.5	5.2	5.5	5.5	5.6	6.8	7.9	-7.8	-5.8	5.5	6.0	6.7
Imports	55.4	9.4	6.1	5.0	3.8	3.9	4.0	4.6	1.3	7.6	30.5	11.2	4.3
Government Purchases	6.4	6.3	2.9	3.2	2.3	0.6	1.0	1.7	2.0	-0.3	3.6	4.7	1.5
Consumption (% of GNP)	64.7	65.1	65.3	65.6	65.9	65.8	65.7	65.4	65.1	65.8	64.9	65.7	65.4
Residential Investment (% of GNP)	3.7	3.6	3.6	3.6	3.6	3.6	3.7	3.7	2.6	3.5	3.7	3.6	3.7
Nonresidential Investment (% of GNP)	12.8	12.9	12.8	12.8	12.8	12.8	12.8	12.9	11.3	11.1	12.5	12.8	12.9
Structures (% of GNP)	3.5	3.5	3.5	3.5	3.5	3.5	3.6	3.6	3.6	3.2	3.5	3.5	3.6
Equipment (% of GNP)	9.3	9.3	9.3	9.3	9.3	9.3	9.3	9.3	7.7	7.9	9.0	9.3	9.3
Inventory Change ($ billions)	68.5	52.9	43.9	30.0	10.8	18.8	22.5	33.1	-26.1	-13.5	61.4	25.9	31.4
Mfg. Capacity Utilization Rate (%)	83	82	82	81	80	80	80	81	71	75	82	81	81
Auto Sales (millions of units)	10.3	10.9	10.9	10.8	10.6	10.5	10.5	10.5	8.0	9.2	10.6	10.7	10.5
Domestic (% of total)	77.3	73.8	77.3	77.0	73.8	72.4	72.2	72.0	72.3	74.0	76.6	75.1	71.5
Imported (% of total)	22.7	26.2	22.7	23.0	26.2	27.6	27.8	28.0	27.9	26.0	23.4	24.9	28.5
Manufacturing Industrial Production (% change)	7.2	1.9	0.7	-0.5	-1.0	1.5	3.1	5.4	-8.5	7.8	11.5	1.8	3.1
Common Market	10.2	2.6	4.7	2.8	3.5	2.9	2.0	3.5	-1.4	0.7	2.9	3.4	2.7
Japan	6.7	8.9	8.8	3.2	2.9	1.5	1.5	2.5	0.4	3.5	10.7	6.3	2.3
Employment(millions)(civilian:household basis)	105.2	106.0	106.4	106.7	107.0	107.4	107.9	108.3	99.5	100.8	105.0	106.9	108.7
Unemployment Rate (%) (civilian)	7.5	7.4	7.5	7.6	7.8	8.0	8.0	8.0	9.7	9.6	7.6	7.7	7.9
Personal Income per Household (average)<1>	38,919	39,507	40,121	40,523	40,859	41,461	42,167	42,997	33,653	35,415	38,539	40,741	43,371
Percent Change -- Year Ago (w/o inflation)	5.9	4.6	3.3	2.0	1.1	1.0	0.8	1.5	-0.5	1.5	5.3	1.9	1.8
Personal Taxes per Household (average)	7,025	7,124	7,231	7,319	7,389	7,527	7,657	7,854	6,434	6,478	6,945	7,367	7,936
Percent Change -- Year Ago (w/o inflation)	6.0	4.8	3.5	2.2	1.3	1.5	1.6	2.6	-2.2	-3.0	3.3	2.1	2.9
Percent of Personal Income	18.8	18.8	18.8	18.9	18.9	19.0	19.0	19.1	19.9	19.1	18.8	18.9	19.1
Disposable Income per Household (average)	31,894	32,383	32,889	33,204	33,469	33,934	34,510	35,143	27,219	28,938	31,594	33,374	35,434
Percent Change--Year Ago (w/o inflation)	5.7	4.5	3.3	2.1	1.2	0.9	0.8	1.3	-0.1	2.5	5.7	1.9	1.6
Household Interest Payments (% of total)	10.5	10.4	10.2	10.3	10.6	10.6	10.4	10.4	9.6	9.8	10.4	10.4	10.3
Net Worth per Household (average)	77,282	78,778	79,790	80,821	82,178	83,700	85,536	87,756	66,105	73,841	76,928	81,622	88,826
Percent Change -- Year Ago (w/o inflation)	-0.6	0.9	1.7	2.4	2.4	2.1	2.8	3.9	-1.9	7.6	0.4	2.1	4.0
Consumer Price Inflation (CPI)	3.6	4.4	3.9	3.9	4.0	4.5	5.0	5.1	6.2	3.2	4.3	4.0	4.8
Gross National Product Inflation (GNP Deflator)	3.7	3.8	4.2	3.7	3.8	4.7	4.8	4.9	6.0	3.8	3.8	3.9	4.6
Personal Consumption Inflation	4.3	4.0	3.4	3.6	3.9	4.4	4.7	4.8	5.9	3.7	3.3	3.7	4.5
Residential Construction Inflation	4.5	0.9	2.8	4.3	4.5	5.1	5.9	6.5	3.0	1.7	3.9	3.8	5.7
Nonresidential Construction Inflation	2.0	2.5	4.4	4.9	5.5	6.1	6.7	7.0	4.9	-1.0	0.4	4.0	6.5
Producers Price Inflation (WPI)	-0.7	-0.1	1.5	2.1	3.3	4.8	5.4	5.4	2.0	1.3	2.4	1.5	4.9
Compensation per Manhour (% change)	3.6	4.0	7.8	6.5	6.2	7.0	7.9	7.2	8.0	4.8	4.2	5.8	7.2
Productivity (% change)	0.0	1.1	1.2	1.3	1.5	1.9	1.7	1.8	0.2	3.4	2.8	1.4	1.7
Unit Labor Cost (% change)	3.9	2.6	6.5	5.1	4.7	5.0	6.1	5.3	7.8	1.3	1.4	4.3	5.4
Unit Capital Cost (% change)	4.4	4.2	4.0	3.7	3.5	3.3	3.2	3.0	9.5	6.9	4.6	3.6	3.0
Before Tax Corporate Profits ($ billions)<2>	231	224	215	214	206	207	212	225	181	213	240	211	228
Corporate Tax Liability	92	89	85	83	78	79	85	92	76	86	96	81	94
After Tax Profits	139	134	130	131	128	128	128	133	105	127	144	129	135
Inventory Valuation Adjustment	0	0	-5	-10	-15	-22	-26	-27	-9	-11	-5	-13	-28
Capital Consumption Adjustment	58	63	72	76	79	83	84	85	3	33	55	78	85
Profits from Current Production (with IVA, CCA)	197	198	197	197	192	190	186	191	98	149	194	194	191
Adjusted for Inflation (84:1 base)	194	192	190	188	182	178	172	175	105	153	191	184	174
Percent Change - Year Ago	18.3	8.5	2.6	-2.8	-6.2	-7.6	-9.2	-7.3	-14.6	46.0	25.0	-3.6	-5.8
Per Unit of Output (% of GNP)	5.3	5.3	5.2	5.1	4.9	4.8	4.6	4.6	3.2	4.5	5.3	5.0	4.6
Effective Corporate Tax Rate (%)<2>	30	30	29	28	28	28	30	31	39	34	32	28	32
Federal Tax Receipts (Unified basis)	701	636	639	822	726	670	664	923	609	613	676	714	776
Percent of GNP	19.0	17.0	16.8	21.3	18.7	16.9	16.4	22.3	19.8	18.6	18.5	18.4	18.6
Federal Expenditures (Unified basis)	833	892	928	939	927	961	988	999	740	803	852	939	1,007
Percent of GNP	22.6	23.8	24.4	24.4	23.8	24.3	24.5	24.2	24.1	24.3	23.3	24.2	24.1
Surplus or Deficit (Unified basis)	-133	-256	-288	-117	-201	-251	-324	-76	-131	-190	-176	-224	-231
% of GNP	3.6	6.8	7.6	3.0	5.2	7.4	8.0	1.8	4.2	5.8	4.8	5.8	5.5
% of Personal Savings	80.7	159.3	176.1	74.8	137.9	192.2	201.4	44.9	97.8	158.1	112.6	145.3	139.3
% of Net Domestic Savings	40.7	79.5	89.2	37.3	68.1	98.0	106.5	23.8	67.3	80.0	55.2	73.1	73.3

<1> Includes personal contributions for social insurance.
<2> Adjusted to include impact of windfall profits tax on domestic crude oil production.

Source: Model developed by the NATIONAL ASSOCIATION OF REALTORS, and Data Resources, Inc,
Assumptions and simulations by Dr. Jack Carlson, Hugh Graham, and Dick Peach.